IP 01-1103-C H/K Shepard v. Humke
Judge David F. Hamilton Signed on 7/9/02

NOT INTENDED FOR PUBLICATION IN PRINT

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF INDIANA
INDIANAPOLIS DIVISION

SHEPARD, GREGORY M, Plaintiff, vs. HUMKE, RAMON L, OMAN, NORMA J, BARNETTE JR, JOSEPH D, SAMS, THOMAS H, PRICE, JAMES D, ROWLAND, SARAH W, KIRR, DAVID M, HACKETT, JOHN T, STATE AUTOMOBILE MUTUAL INSURANCE COMPANY, STATE AUTO FINANCIAL CORPORATION, MERIDIAN INSURANCE GROUP INC, Defendants.	)	CAUSE NO. IP01-1103-C-H/G

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UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF INDIANA
INDIANAPOLIS DIVISION

GREGORY M. SHEPARD and AMERICAN UNION INSURANCE COMPANY, Plaintiffs, v. RAMON L. HUMKE, NORMA J. OMAN, JOSEPH D. BARNETTE, JR., THOMAS H. SAMS, JAMES D. PRICE, SARAH W. ROWLAND, DAVID M. KIRR, and JOHN T. HACKETT, STATE AUTOMOBILE MUTUAL INSURANCE COMPANY, STATE AUTO FINANCIAL CORPORATION, and MERIDIAN INSURANCE GROUP, INC., Defendants.	)	CAUSE NO. IP 01-1103-C H/K

ENTRY ON DEFENDANTS' MOTION TO DISMISS

This diversity action is the second attempt by plaintiff Gregory M. Shepard to challenge the merger of Meridian Insurance Group, Inc. ("MIGI") and a wholly owned subsidiary of State Automobile Mutual Insurance Company ("State Auto"). The merger was consummated on or about June 1, 2001. It left MIGI as the surviving entity, as a subsidiary of State Auto.

Prior to the MIGI-State Auto merger, Shepard owned about 20 percent of MIGI common stock. He had made repeated attempts to acquire MIGI through plaintiff American Union Insurance Company, which he controlled. Shepard first brought an action to enjoin the merger between MIGI and State Auto in *Shepard v. Meridian Insurance Group, Inc. et al.*, Cause No. IP00-1360-C H/G. The court dismissed that action on April 10, 2001 on the grounds that the "dissenters' rights" provisions of the Indiana Business Corporation Law, Indiana Code § 23-1-44-8(c), foreclosed the injunctive relief Shepard sought. *Shepard v. Meridian Insurance Group, Inc.*, 137 F. Supp. 2d 1096 (S.D. Ind. 2001). The court also concluded that any claim Shepard had for damages arising from the merger was not ripe before the merger's consummation. *Id.* at 1113-14.

Now that the merger has been completed, plaintiff Shepard has returned to court seeking monetary relief. His amended complaint asserts three claims. Count I, against the directors of MIGI, alleges violations of the directors' fiduciary duties in negotiating and approving the State Auto merger. Count II, against State Auto Mutual and State Auto Financial alleges breach of a confidentiality agreement governing the exchange of certain business information regarding

possible acquisition of MIGI.[1] Count III against MIGI itself and director and officer Norma J. Oman alleges tortious interference with contract based on State Auto's alleged breach of the confidentiality agreement. Plaintiff American Union has joined the tortious interference claim. Defendants have moved to dismiss all of plaintiffs' claims under Rule 12(b)(6) of the Federal Rules of Civil Procedure for failure to state a claim upon which relief could be granted. As explained below, the defendants' motion is denied.

Dismissal Standard

In deciding a motion to dismiss under Rule 12(b)(6), the court reviews all facts alleged in the complaint and any inferences reasonably drawn from the alleged facts in the light most favorable to the plaintiff. *E.g.*, *Gould v. Artisoft, Inc.*, 1 F.3d 544, 548 (7th Cir.1993) (reversing dismissal). Dismissal is warranted only if the plaintiff can prove no set of facts consistent with the complaint that would entitle her to relief. *Hishon v. King & Spalding*, 467 U.S. 69, 73 (1984); *Conley v. Gibson*, 355 U.S. 41, 45-46 (1957). Detailed allegations of facts, legal theories, or their elements are not required in the complaint. Under Rule 8(a) of the Federal Rules of Civil Procedure, all that is needed is "a short and plain

[1]Although identified as separate entities, the defendants have not treated the two State Auto entities differently for purposes of their motion to dismiss. In the pleadings and briefs, the parties sometimes referred to "State Auto" without distinguishing between State Auto Mutual and State Auto Financial.

statement of the claim showing that the pleader is entitled to relief." "A complaint does not fail to state a claim merely because it does not set forth a complete and convincing picture of the alleged wrongdoing." *Bennett v. Schmidt*, 153 F.3d 516, 518 (7th Cir. 1998) (reversing dismissal of employment discrimination complaint).

Plaintiffs have attached several exhibits to their amended complaint. The court may consider these documents in evaluating the defendants' motion to dismiss. See Fed. R. Civ. P. 10(c) (a copy of any written instrument which is an exhibit to a pleading is a part thereof for all purposes); see also *Menominee Indian Tribe v. Thompson*, 161 F.3d 449, 456 (7th Cir. 1998) (in deciding motion to dismiss, district court could properly rely on documents referred to in complaint but not attached to complaint). Thus, "[a] plaintiff may plead himself out of court by attaching documents to the complaint that indicate that he or she is not entitled to judgment." *Matter of Wade*, 969 F.2d 241, 249 (7th Cir. 1992) (citation omitted).

Background

The facts stated here are taken from the amended complaint or are not inconsistent with it. Many of these same facts also were summarized in *Shepard I*, 137 F. Supp. 2d at 1097 - 99.

Defendant Meridian Insurance Group, Inc. ("MIGI"), is an Indiana corporation that has its principal place of business in Indianapolis, Indiana. MIGI is an insurance holding company. At the time of the events alleged in the complaint, defendants Ramon L. Humke, Norma L. Oman, Joseph D. Barnette, Jr., Thomas H. Sams, James D. Price, Sarah W. Rowland, David M. Kirr, and John T. Hackett were all directors of MIGI. Humke also served as chairman of the board and Oman was MIGI's president and CEO.

Defendants State Automobile Mutual Insurance Company and State Auto Financial Corporation are Ohio corporations with their principal place of business in Columbus, Ohio.

Effective on or about June 1, 2001, MIGI was merged with a wholly owned subsidiary of State Auto, with MIGI being the surviving corporation. As a result of the merger, MIGI is now a wholly owned subsidiary of State Auto.

Plaintiff Gregory M. Shepard owned about 20 percent of MIGI shares prior to the merger. Shepard is a 50% shareholder as well as the President and Chairman of American Union Insurance Company, an Illinois stock insurance company. Both plaintiffs are citizens of Illinois; no defendant is a citizen of Illinois for purposes of the court's diversity jurisidiction.

On August 30, 2000 and September 18, 2000, Shepard made tender offers for the control of MIGI through American Union. The MIGI directors recommended that MIGI shareholders turn down Shepard's offers. They later recommended that the shareholders accept a tender offer from State Auto, which resulted in the June 1, 2001 merger described above. Shepard's and American Union's claims are based on actions taken by MIGI and its directors in response to the Shepard's and State Auto's attempts to acquire MIGI.

On August 29, 2000, MIGI stock traded for $12.75 per share. On August 30, 2000, Shepard announced his intention to commence a tender offer for 100 percent of MIGI shares for a price of $20 per share.

On September 8, 2000, MIGI's board of directors met and decided to recommend to MIGI shareholders that they reject Shepard's tender offer. The board followed that decision with a September 11, 2000 letter to all shareholders

asserting that the offer price was inadequate and did not reflect the inherent value of the company. The board also wrote in its letter:

> Based on Shepard's past history and experience in the insurance industry, it would not be in the best interests of the Company or its shareholders, employees, agents and policyholders and would be detrimental to the long-term viability of the Company for Shepard to obtain control. Specifically, the Board is concerned with Shepard's involvement in the recent insolvency of Illinois HealthCare Insurance Company, as noted above.

Am. Cplt. ¶ 46, Ex. 5.

On September 18, 2000, Shepard announced that he was amending his tender offer. Instead of seeking all MIGI shares, his September tender offer sought only 50.1 percent of the shares, but he increased the offered price to $25 per share.

The MIGI board met and decided to recommend that shareholders also reject Shepard's September tender offer. On September 22, 2000, the board again wrote to shareholders with that recommendation, emphasizing again Shepard's "past history and experience in the insurance industry." Am. Cplt. ¶ 51, Ex. 7. That factor, said the board, took on greater significance for shareholders because the tender for only 50.1 percent of shares would leave 49.9 percent of shares held by minority shareholders in a company controlled by

Shepard. The board also advised shareholders that holders of more than 50 percent of MIGI shares had indicated they would reject the tender offer. Am. Cplt., Ex. 7. (Nearly 50 percent of MIGI shares were held by Meridian Mutual Insurance Company, which was well-represented on the MIGI board.)

On September 25, 2000, the Indiana Securities Commissioner held a hearing to evaluate the disclosures related to Shepard's tender offers. On October 4, 2000, the Commissioner issued a decision requiring Shepard to make additional disclosures of financial and accounting information. The Commissioner did not, however, issue a cease-and-desist order.

The next day, after learning that the Securities Commissioner would not block Shepard's tender offer, the MIGI board issued a press release announcing that the board had directed management "to explore strategic alternatives to enhance shareholder value." Am. Cplt. ¶ 70. The alternatives included a variety of transactions, including possible mergers with third parties. The press release added: "The Board reconfirmed that the Company has no interest in engaging in any transaction with American Union Insurance Company, Gregory M. Shepard or any of their respective affiliates."

On October 2, 2000, Shepard met with Robert Bailey, chairman of State Auto, to discuss matters relating to Shepard's interest in MIGI. Am. Cplt. ¶ 57. On behalf of State Auto, Bailey entered a confidentiality agreement regarding the confidential information he and Shepard discussed. Am. Cplt. ¶ 58, Ex. 8. Among other things, the agreement prohibited State Auto from disclosing confidential information it obtained from Shepard and from trading in MIGI stock as a result of the disclosure of confidential information.

On October 6, 2000, Shepard responded to the MIGI press release with his own announcement stating his intention to press forward with his tender offer despite the MIGI board's rejection of his efforts.

Also on October 6, 2000, MIGI and State Auto entered into an agreement for the exchange of confidential business information as a precursor to negotiating a merger or combination. Less than three weeks later, on October 25, 2000, MIGI announced that it had entered into a merger agreement with State Auto and a wholly owned subsidiary of State Auto known as "MIGI Acquisition." This is the merger that was consummated effective June 1, 2001.

Under the merger agreement, public shareholders of MIGI were paid $30 per share, for a total payment of more than $100 million. MIGI survived the merger as a wholly owned subsidiary of State Auto.

The State Auto merger agreement included a so-called "break-up fee" of $25 million plus State Auto's expenses related to the deal. In addition, the agreement contained a "no solicitation" provision that Shepard contends sharply restricted the MIGI board's ability to entertain any competing offers for the company. Shepard has alleged that any competing bidder would have had to pay at least $35 per share before it could even match the value of the State Auto bid as protected by the break-up fee.

The merger deal also included a voting agreement under which Meridian Mutual agreed to vote its 48.6 percent of MIGI shares in favor of the State Auto merger and against approval of any other merger or business combination, except under certain conditions. State Auto also owned shares of MIGI, and State Auto's Schedule 13D filed with the SEC indicates it controlled 54.6 percent of MIGI shares, including the Meridian Mutual shares.

In *Shepard I*, defendants had projected that Shepard would receive $47,652,000 in cash for his MIGI shares under the State Auto merger. Those

same shares had a market value of just $20,252,100 the day before Shepard announced his first tender offer on August 30, 2000.

Additional facts (or allegations of fact) are included below, keeping in mind the standard for deciding a motion to dismiss.

Discussion

MIGI is an Indiana corporation, so its internal affairs are governed by Indian a law. See *CTS Corp. v. Dynamics Corp. of America*, 481 U.S. 69, 89 (1987) ("No principle of corporation law and practice is more firmly established than a State's authority to regulate domestic corporations, including the authority to define the voting rights of shareholders."), citing Restatement (Second) of Conflict of Laws § 304 (1971).[2]

I. *Breach of Fiduciary Duty*

Plaintiff Shepard alleges that the MIGI directors and officers breached their fiduciary duty to shareholders by opposing Shepard's tender offers in favor of

[2]As an initial matter, defendants have argued, as they did in *Shepard I*, that plaintiffs' action should be dismissed because their claims could be brought, if at all, as a derivative action. The argument certainly has respectable support, but the court rejected this argument in *Shepard I*, 137 F. Supp. 2d at 1109-12. The court's view on the issue has not changed.

State Auto's. Defendants contend that plaintiffs' allegations cannot survive a motion to dismiss because (a) the allegations are barred by the doctrine of judicial estoppel; (b) the allegations do not support a breach of fiduciary duty claim; and (c) the allegations do not support an inference that the directors acted with a state of mind sufficient to defeat the business judgment rule.

A. *Judicial Estoppel & Shepard I*

The court begins its analysis of the breach of fiduciary claim by considering both parties' arguments that the resolution of defendants' motion is a foregone conclusion based on the prior actions of the plaintiff or of this court. Defendants invoke judicial estoppel, while plaintiffs invoke the law of the case. Both arguments fail. The breach of fiduciary duty claim stands or falls on its own in this case.

1. *Judicial Estoppel*

Defendants contend that plaintiffs are judicially estopped from claiming that $30 per share (the price State Auto paid) was not an adequate price for MIGI shares because plaintiffs previously took the position before this court that $20 per share (the price Shepard offered initially) was such a good price that the MIGI directors could not oppose plaintiffs' tender offer without breaching their fiduciary duties. Defendants also contend that judicial estoppel precludes plaintiffs' current action because the Indiana Securities Commissioner did not block plaintiffs' offer. Defendants' judicial estoppel argument fails because Shepard never persuaded this court or the Commissioner to adopt a position that is inconsistent with his position here.

The Supreme Court discussed judicial estoppel in *New Hampshire v. Maine*, 532 U.S. 742 (2001):

> Courts have observed that "[t]he circumstances under which judicial estoppel may appropriately be invoked are probably not reducible to any general formulation of principle," *Allen [v. Zurich Ins. Co.*, 667 F.2d 1162, 1166 (4th Cir. 1982)]; accord *Lowery v. Stovall*, 92 F.3d 219, 223 (C.A.4 1996); *Patriot Cinemas, Inc. v. General Cinema Corp.*, 834 F.2d 208, 212 (C.A.1 1987). Nevertheless, several factors typically inform the decision whether to apply the doctrine in a particular case: First, a party's later position must be "clearly inconsistent" with its earlier position. *United States v. Hook*, 195 F.3d 299, 306 (C.A.7 1999); *In re Coastal Plains, Inc.*, 179 F.3d 197, 206 (C.A.5 1999); *Hossaini v. Western Mo. Medical Center*, 140 F.3d

> 1140, 1143 (C.A.8 1998); *Maharaj v. Bankamerica Corp.*, 128 F.3d 94, 98 (C.A.2 1997). Second, courts regularly inquire whether the party has succeeded in persuading a court to accept that party's earlier position, so that judicial acceptance of an inconsistent position in a later proceeding would create "the perception that either the first or the second court was misled," *Edwards* [*v. Aetna Life Ins. Co.*, 690 F.2d 595, 599 (6th Cir. 1982)]. Absent success in a prior proceeding, a party's later inconsistent position introduces no "risk of inconsistent court determinations," *United States v. C.I.T. Constr. Inc.*, 944 F.2d 253, 259 (C.A.5 1991), and thus poses little threat to judicial integrity. See *Hook*, 195 F.3d, at 306; *Maharaj*, 128 F.3d, at 98; *Konstantinidis* [*v. Chen*, 626 F.2d 933, 939 (D.C. Cir. 1980)]. A third consideration is whether the party seeking to assert an inconsistent position would derive an unfair advantage or impose an unfair detriment on the opposing party if not estopped. See *Davis* [*v. Wakeless*, 156 U.S. 680, 689, 15 S.Ct. 555 (1895)]; *Philadelphia, W., & B.R. Co. v. Howard*, 13 How. 307, 335-337, 14 L.Ed. 157 (1851); *Scarano* [*v. Central R. Co. of New Jersey*, 203 F.2d 510, 513 (3d Cir. 1953)] (judicial estoppel forbids use of "intentional self-contradiction . . . as a means of obtaining unfair advantage"); see also 18 Wright § 4477, p. 782.
>
> In enumerating these factors, we do not establish inflexible prerequisites or an exhaustive formula for determining the applicability of judicial estoppel. Additional considerations may inform the doctrine's application in specific factual contexts.

532 U.S. at 750-51.

Indiana courts generally have followed the same judicial estoppel principles, including the need for prior success with the inconsistent position. In *Meridian Ins. Co. v. Zepeda*, the Indiana Court of Appeals described the doctrine:

> Judicial estoppel "prevents a party from asserting a position in a legal proceeding inconsistent with one previously asserted." *Wabash Grain, Inc. v. Smith*, 700 N.E.2d 234, 237 (Ind. Ct. App.1998). Litigants are prohibited from taking advantage of the judicial process by prevailing twice under different theories. *GEICO Ins. Co. v. Rowell*, 705 N.E.2d 476, 481 (Ind. Ct. App.1999), *reh'g denied*. Judicial estoppel prevents a party who has successfully maintained a position in the first proceeding from subsequently asserting an inconsistent position. *The key to the doctrine is that it prohibits a party from presenting a position contrary to one upon which he previously prevailed.* See 31 C.J.S. Estoppel and Waiver § 139(b)(1996).

734 N.E.2d 1126, 1132 (Ind. App. 2000) (emphasis added). See also *Allstate Ins. Co. v. Dana Corp.*, 737 N.E.2d 1177, 1193-94 (Ind. App. 2001) (reversing trial court's application of judicial estoppel because, although plaintiff changed positions in subsequent litigation, it had not prevailed on different position in earlier litigation), *aff'd in relevant part*, 759 N.E.2d 1049, 1063 (Ind. 2001); *Cooper v. Eagle River Memorial Hosp., Inc.*, 270 F.3d 456, 462-63 (7th Cir. 2001) (applying Wisconsin law: "To invoke judicial estoppel, a court must identify three elements (1) the later position must be clearly inconsistent with the earlier position; (2) the facts at issue should be the same in both cases; and (3) the party to be estopped must have convinced the first court to adopt its position); *DeVito v. Chicago Park Dist.*, 270 F.3d 532, 535 (7th Cir. 2001) (judicial estoppel "forbids a party who has won a case on one ground to turn around in a subsequent case and repudiate that ground in an effort to win a second victory."). The doctrine applies to administrative as well as judicial proceedings. See *Chaveriat v.*

Williams Pipe Line Co., 11 F.3d 1420, 1427 (7th Cir. 1993) ("Though called judicial estoppel, the doctrine has been applied, rightly in our view, to proceedings in which a party to an administrative proceeding obtains a favorable order that he seeks to repudiate in a subsequent judicial proceeding.").

Defendants base their judicial estoppel argument in part on allegations in Shepard's original complaint in *Shepard I.* In that complaint, Shepard alleged that the MIGI directors breached their fiduciary duty by rejecting his tender offer. Shepard asked the court to enjoin the MIGI directors from rejecting his offer. See *Shepard I,* Cplt., ¶¶ 51-56, 106-107, and prayer for relief. Shepard filed his original complaint in *Shepard I* on August 30, 2000, the same day he made his original tender offer. Shepard amended his complaint in *Shepard I* on December 8, 2000, after MIGI had rejected his second tender offer and entered an agreement with State Auto. The amended complaint in *Shepard I* did not allege that the directors breached their fiduciary duty by rejecting Shepard's offer. Nor did it seek injunctive relief to enforce his tender offer. Instead, Shepard sought an injunction to block the consummation of MIGI's merger with State Auto.

The fact that Shepard once took a position in *Shepard I* that seems inconsistent with the position he asserts here may provide ample fuel for

arguments and cross-examination at later stages, but it does not provide a basis for invoking judicial estoppel. Shepard never prevailed on the theory that the MIGI directors violated their fiduciary duty by rejecting his tender offer at $20.

Defendants also contend that the proceedings before the Indiana Securities Commissioner provide a basis for judicial estoppel. The defendants' premise is that Shepard "prevailed" before the Commissioner because the Commissioner did not issue a cease and desist order to block his tender offer. Instead, the Commissioner only ordered Shepard to supplement his financial disclosures. This result is not tantamount to Shepard persuading the Commissioner to adopt a position that is inconsistent with his position here. The Commissioner ordered Shepard to disclose more information about his ability to pay the price offered but did not pass judgment on the adequacy of the price per share in the tender offer.

The defendants make much out of the fact that Shepard provided his press releases about the tender offer to the Commissioner and that those press releases represented that Shepard's $20 per share offer was in the MIGI shareholders' "interest." But there is no indication that the Commissioner's action requiring additional financial disclosures had anything to do with the price Shepard offered. The Securities Commissioner's Findings of Fact, Conclusion of

Law, and Final Order stated that the "sole purpose of the hearing [before the Securities Division] was to determine, by a preponderance of the evidence, whether the takeover statement fails to provide full and fair disclosure to the offerees of all material information concerning the takeover offer . . ." Findings of Fact ¶ 13 (internal quotation and citation omitted). The Commissioner emphasized that he was considering only whether the takeover statement made a full and fair disclosure. See Conclusions of Law ¶ 7 ("Simply stated, given the evidence presented at the hearing, and the parties' above-described stipulations, the Securities Commissioner must determine whether the takeover statement filed by offerors fully and fairly discloses to the offerees all material information concerning the offer."). Thus, the Securities Commissioner's actions do not provide a basis for judicial estoppel against Shepard based on his $20 per share offer because the Commissioner never agreed with Shepard about the price offered.

2. *Shepard I*

Plaintiff Shepard contends that the defendants' motion to dismiss his fiduciary duty claim must be denied because this court already decided in *Shepard I* that Shepard's allegations state a claim on which relief can be granted. Plaintiffs rely on the following language from the court's earlier decision:

> This substantive protection [of the business judgment rule] for directors is extensive, but not absolute. In deciding defendants' motion to dismiss under Rule 12(b)(6), therefore, *the court must assume that plaintiff Shepard would be able to prove that the defendant directors willfully or recklessly breached their duties in deciding to approve the State Auto merger.*

Shepard, 137 F. Supp. 2d at 1103 (emphasis added). The court also stated:

> If and when the merger is completed, Shepard might be able to pursue a direct action against the directors for monetary relief for an alleged breach of their duty to shareholders, though his claim would confront the highly deferential business judgment rule under Indiana law, see generally Ind. Code § 23-1-35-1 (business judgment rule), *and it is not clear whether Indiana law would recognize such claims even then*.

Id. at 1097(emphasis added).

As the language in the second passage makes clear, the language from *Shepard I* in the first passage quoted above does not establish as the "law of the case," issue preclusion, or on any other basis that Shepard can state a claim for damages against the directors based on an alleged breach of fiduciary duty. The issue presented in *Shepard I* was whether injunctive relief was available to block the proposed merger transaction, or whether the dissenters' rights provisions of the Indiana Business Corporation Law foreclosed such injunctive relief. The defendants' position against such relief was built upon arguments that would

apply even to egregious cases of director misconduct. In light of the broad sweep of the arguments presented, the court assumed, for purposes of analyzing the issue of relief, that a breach of directors' fiduciary duty could be shown. Nothing more should be inferred from the quoted statement. In this action, the substance of Shepard's claim is at issue, not the appropriate remedy. The court simply did not reach the merits of the breach of fiduciary claim in *Shepard I.*

B. *Breach of Fiduciary Duty – Shepard's Allegations*

Turning to the substance of Shepard's breach of fiduciary duty claim, the defendants contend that Shepard's allegations do not state a claim because he has not alleged conduct that constitutes a breach or violates the business judgment rule. The court denies the defendants' motion to dismiss the breach of fiduciary duty claim because, drawing all reasonable inferences in plaintiff's favor, his allegations state a claim upon which relief could be granted.

As this court discussed in *Shepard I*, Indiana has adopted by statute "a strongly pro-management version of the business judgment rule." See *G&N Aircraft, Inc. v. Boehm*, 743 N.E.2d 227, 238 (Ind. 2001) (describing Ind. Code § 23-1-35-1(e)). A director has a duty under the law to act in good faith, with ordinary care under the circumstances, and in a manner the director believes to

be in the best interests of the corporation. Ind. Code § 23-1-35-1(a). Individual director liability requires proof that a director not only breached a duty of good faith and ordinary care, but that the breach or failure to perform constituted "willful misconduct or recklessness." Ind. Code § 23-1-35-1(e); *G&N Aircraft*, 743 N.E.2d at 238; *Shepard*, 137 F. Supp. 2d at 1103. The official study commission comment on the business judgment statute states that director liability for damages requires proof of, "at a minimum, conscious disregard or indifference to the consequences of a risky act." Ind. Code § 23-1-35-1(e).[3]

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[3]The Supreme Court of Indiana has recognized the commission's commentary as authoritative. *Fleming v. International Pizza Supply Corp.*, 676 N.E.2d 1051, 1054 n.5 (Ind. 1997). The commentary to subsection (e) further explains:

> Subsection (e)'s liability standard is a conscious response to the serious problems that have arisen in recent years due to the increasing amount of litigation against directors, the increasing expense of defending such claims, and the increasing cost (and decreasing availability and scope) of director and officer liability insurance. These developments have in turn made it increasingly difficult for corporations to persuade qualified individuals to serve on boards of directors. Narrowing the bases for imposition of personal liability on directors was recommended by the Commission, and adopted by the General Assembly, as a crucial part of Indiana's efforts to reverse that trend. Subsection (e) reflects the public policy of Indiana that personal liability should be imposed on directors only in limited circumstances, and should be construed in furtherance of that objective.

While this substantive protection for directors is extensive, it is not absolute. Shepard alleges that the MIGI directors breached their fiduciary duty because they: (1) had unwarranted "antipathy" towards Shepard; (2) wanted to ensure that Oman and Steven Hazelbaker would obtain the positions of Vice Chairman and President, respectively, following the merger with State Auto; (3) made misrepresentations about their decisions regarding merger negotiations; (4) failed to obtain the highest possible price for MIGI shares, including by establishing a break-up fee that would dissuade other potential purchasers; and (5) improperly relied on confidential information that plaintiffs had disclosed to State Auto, giving State Auto an unfair advantage over plaintiffs.

Although one may be skeptical about the merits of Shepard's breach of fiduciary claim in light of the broad protections of the business judgment statute, taken as a whole, his allegations are sufficient to survive a motion to dismiss. For example, Shepard's allegations regarding the directors' misrepresentations and the break-up fee are the sort of allegations that could sustain a breach of fiduciary claim if supported with evidence that the directors deliberately chose not to act in the best interests of the corporation's multiple constituencies or were indifferent to the interests of those constituencies. The court reserves its analysis of Shepard's multiple breach of fiduciary duty theories until later stages of the proceedings, when a record of actual evidence will be available. The court

cannot say at this stage that there is no possible set of facts consistent with the allegations in Shepard's complaint that would permit him to prove a breach of fiduciary duty. Shepard is entitled to attempt to develop this claim in discovery, keeping in mind his obligations under Rule 11 of the Federal Rules of Civil Procedure. As the Supreme Court explained recently: "Rule 8(a) establishes a pleading standard without regard to whether a claim will succeed on the merits. 'Indeed it may appear on the face of the pleadings that a recovery is very remote and unlikely but that is not the test.'" *Swierkiewicz v. Sorema N. A.*, 122 S. Ct. 992, 999 (2002), quoting *Scheuer v. Rhodes*, 416 U.S. 232, 236 (1974).

II. *Breach of Contract*

Plaintiffs Shepard and American Union allege that defendants State Auto Mutual and State Auto Financial breached a confidentiality agreement with them in negotiating and consummating the MIGI merger. The agreement is contained in a letter written by Shepard on American Union letterhead. See Am. Cplt., Ex. 8. Robert Bailey signed the letter agreement for State Auto Financial. The agreement provided that State Auto Financial would not disclose "Confidential Information" obtained from American Union, which was defined as information that was "non-public, confidential and/or proprietary." The letter agreement limited the definition of "Confidential Information" with the following language:

> The restrictions set forth in this letter shall not apply to any part of the Confidential Information (a) in the public domain not as a result of the violation of Recipient's [State Auto's] undertaking herein, (b) available to Recipient prior to disclosure of it to Recipient, (c) hereafter made available to Recipient from another source, provided that such source in so acting is not to Recipient's knowledge violating any duty or agreement of confidentiality, (d) required to be disclosed pursuant to any law, legal process, or judicial or governmental circumstances or stock exchange rule, (e) independently developed by Recipient without the use of the Confidential Information, or (f) disclosed to others on an unrestricted or non-confidential basis.

In addition to prohibiting the disclosure of Confidential Information, the agreement also provided:

> Recipient [State Auto] hereby agrees not to trade in any securities of MIGI as a result of disclosure of the Confidential Information, or any other information disclosed by the Company, until forty-eight (48) hours after the public disclosure of such Confidential Information or other information was made by the Company.

Defendants argue that plaintiffs cannot state a claim for breach of contract because (1) plaintiffs have not alleged the disclosure of "Confidential Information" as that term is defined in the agreement; and (2) the agreement's prohibition against "trading" MIGI securities did not apply to prohibit the MIGI merger.

The complaint alleges that Shepard met with Bailey on October 2, 2000 and discussed his analysis of the value of MIGI. Shepard told Bailey that he believed the value was significantly more than $44.59 per share. Am. Cplt. ¶ 63.

Shepard also told Bailey that he did not alone have the resources to offer significantly more than the $25.00 per share for 50.1 percent of MIGI's outstanding shares of common stock that he had already offered to buy. Shepard proposed a joint venture in which Shepard would acquire shares of MIGI at $27 per share with State Auto's help with financing. In exchange, State Auto would have the option to acquire MIGI in one year at a price of $40 per share. In addition, Shepard showed Bailey documents that Shepard had created and labeled "CONFIDENTIAL." The documents included data supporting Shepard's analysis of the value of MIGI, a document noting the alternatives available to MIGI, and a document outlining the proposal made to Shepard regarding State Auto acquiring an option to purchase Shepard's shares of MIGI common stock at $40. Am. Cplt. ¶¶ 63-64.

Defendants contend that none of the information allegedly disclosed was confidential under the agreement. Specifically, defendants assert that Shepard's valuation of MIGI stock was not confidential because it was based on publicly available financial information. In addition, the alternatives Shepard outlined – such as MIGI finding a "white knight" – were generally known as alternatives in many merger scenarios. Defendants also discount Shepard's disclosure of information about his financial situation because he was required by the SEC to make certain financial disclosures with his tender offer and amended tender

offer. With respect to the prohibition against trading MIGI stocks based on Confidential Information, defendants argue that MIGI stocks were not "traded" under the State Auto merger agreement because the sale of shares was not voluntary – under the agreement, stockholders were forced to sell.

The court denies the defendants' motion to dismiss plaintiffs' breach of contract claim. The defendants' arguments go the merits of the plaintiffs' claim and they may be appropriate for consideration on summary judgment. The court cannot say that the claim fails based on the face of the complaint and the letter agreement attached to the complaint. The plaintiffs are entitled to attempt to develop their theory that Shepard disclosed information to State Auto that was confidential under the agreement, the existence of which defendants do not dispute, at least for purposes of their motion to dismiss.

III. *Tortious Interference with Contract*

Plaintiffs Shepard and American Union base their tortious interference claim against MIGI and Oman on alleged interference with the confidentiality agreement between plaintiffs the State Auto defendants, discussed above. To prove tortious interference with contract under Indiana law, a party must show: (1) the existence of a valid and enforceable contract; (2) the defendant's

knowledge of that contract; (3) the defendant's intentional inducement to breach that contract; (4) the absence of justification; and (5) damages resulting from the breach. *National City Bank, Indiana v. Shortridge*, 689 N.E.2d 1248, 1252 (Ind. 1997); *McLinden v. Coco*, 765 N.E.2d 606, 617 (Ind. App. 2002).

Defendants argue first that the plaintiffs' tortious interference claim is preempted by the Indiana Trade Secrets Act ("ITSA"), Ind. Code § 24-2-3-1 *et seq*. The parties have not cited any decisions on this issue under Indiana law. Defendants rely on the ITSA provision stating that the statute "displaces all conflicting law of this state pertaining to the misappropriation of trade secrets, except contract law and criminal law," Ind. Code § 24-2-3-1(c), and on decisions from the Northern District of Illinois holding that similar tort claims were preempted by the parallel Illinois trade secret statute. See *Automed Technologies, Inc. v. Eller*, 160 F. Supp. 2d 915, 922 (N.D. Ill. 2001); *Leggett & Platt, Inc. v. Hickory Springs Mfg. Co.*, 132 F. Supp. 2d 643, 648-49 (N.D. Ill. 2001), *aff'd in part and rev'd in part on other grounds*, 285 F.3d 1353 (Fed. Cir. 2002); *Thomas & Betts Corp. v. Panduit Corp.*, 108 F. Supp. 2d 968, 974 (N.D. Ill. 2000). The Illinois cases reason that, because the trade secret statute defines misappropriation of a trade secret to include inducing another person to breach a duty to maintain secrecy of trade secrets, the preemption provision means that

the statutory remedy for such inducement displaces any common law tort remedy. (Contract remedies are left intact under this approach.)

The premise for invoking preemption under Ind. Code § 24-2-3-1(c) must be a showing that the tort claim in question deals with "trade secrets" within the meaning of the ITSA. The preemption provision does not purport to apply to all claims for relief for inducing breaches of obligations to maintain secrecy. (Consider, for example, possible claims for inducing an attorney, physician, clergy, or accountant to violate professional obligations of confidentiality. Such claims would not fall within the ITSA preemption provision.) This preemption theory does not necessarily apply to plaintiffs' claim for tortious interference because plaintiffs have not tried to allege that the information they provided to State Auto qualified as trade secrets under the ITSA.

The Indiana preemption provision is limited to "conflicting law of this state pertaining to the misappropriation of trade secrets. . . ." Ind. Code § 24-2-3-1(c). The ITSA defines "trade secret"as "information, including a formula, pattern, compilation, program, device, method, technique, or process, that: (1) derives independent economic value, actual or potential, from not being generally known to, and not being readily ascertainable by proper means by, other persons who can obtain economic value from its disclosure or use; and (2) is the subject of

efforts that are reasonable under the circumstances to maintain its secrecy." Ind. Code § 24-2-3-2. The statutory standard does not draw sharp lines, and it has generated litigation over whether particular types of information are protected by the statute. See, *e.g.*, *Amoco Production Co. v. Laird*, 622 N.E.2d 912, 919 (Ind. 1993) (results of microwave radar search for potential oilfields were protected as trade secrets), reversing *Laird v. Amoco Production Co.*, 604 N.E.2d 1249, 1254 (Ind. App. 1992) (holding such results were not trade secrets protected from misappropriation because competitors could conduct their own surveys); *Ackerman v. Kimball Int'l, Inc.*, 634 N.E.2d 778 (Ind. App. 1994) (customer and supplier lists and pricing information were protected as trade secrets), *aff'd in relevant part*, 652 N.E.2d 507 (Ind. 1995).[4]

Further, even if it were later determined that the plaintiffs' tortious interference claim applied to genuine trade secrets, then the alleged claim could

[4]Parties who wish to avoid such uncertainty have the option of contracting for confidentiality protections that go beyond the statute. Moreover, when a party has genuine trade secrets to protect, it can be vital for such a party to obtain contractual promises of confidentiality before disclosing such information to someone with whom it wants to do business. Compare, *e.g.*, *Trandes Corp. v. Guy F. Atkinson Co.*, 996 F.2d 655, 664 (4th Cir. 1993) (jury could reasonably find that secrecy was not lost where plaintiff's only disclosures of secret object-code version of software were made in confidence under licensing agreements or in licensing negotiations); with *Flotec, Inc. v. Southern Research, Inc.*, 16 F. Supp. 2d 992, 1004-05 (S.D. Ind. 1998) (plaintiff held not entitled to trade secret protection for information it disclosed without securing contractual protection).

fall within the ITSA as a claim for misappropriation of trade secrets by inducing a breach of a duty to maintain secrecy.

Defendants also argue that dismissal of the tortious interference claim is appropriate because plaintiffs cannot prove that the defendants caused any of their alleged damages. This issue simply cannot be resolved on defendants' motion to dismiss.

Conclusion

For the reasons explained above, defendants' motion under Federal Rule of Civil Procedure 12(b)(6) to dismiss plaintiffs' complaint for failure to state a claim is denied. Defendants shall answer the amended complaint no later than August 8, 2002.

So ordered.

Date: July 9, 2002

DAVID F. HAMILTON, JUDGE
United States District Court
Southern District of Indiana

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